

# **SAN DIEGO COUNTY**

Audit Report

## **PROPERTY TAX APPORTIONMENT AND ALLOCATION SYSTEM**

*July 1, 2003, through June 30, 2009*



**JOHN CHIANG**  
California State Controller

September 2010



**JOHN CHIANG**  
**California State Controller**

September 16, 2010

Tracy M. Sandoval  
Auditor and Controller/  
Assistant Chief Financial Officer  
San Diego County  
County Administration Center  
1600 Pacific Highway, Room 166  
San Diego, CA 92101-2478

Dear Ms. Sandoval:

The State Controller's Office (SCO) audited the methods employed by the San Diego County to apportion and allocate property tax revenues for the period of July 1, 2003, through June 30, 2009. The audit was conducted pursuant to the requirements of Government Code section 12468.

As repeatedly identified in our previous reports, our audit found that the county overstated its General Fund revenue base by \$694,500, and thus miscalculated the Fiscal Year (FY) 1978-79 base-year apportionment (SB 154 Split). The county asserts the amount in question is penalties and interest; however, it has been unable to support this assertion. Due to inaction by the county, the amount grew exponentially over the years. As of June 30, 2009, the cumulative effect of the miscalculation was that the county's General Fund received approximately \$109,379,259 more in revenues, while the public schools and special districts did not receive \$101,504,582 and \$7,874,677, respectively, from the county's General Fund.

Under Proposition 98, the state's General Fund is to "backfill" any amount short of the revenue limit for the county's non-basic aid school districts. Based on data available for FY 2007-08 and FY 2008-09, the miscalculation resulted in more than \$78 million in excessive state General Fund contributions to San Diego County's non-basic aid school districts.

As you know, the SCO has disclosed the same concern in three previous audit reports dated September 20, 1991; May 30, 1997; and June 9, 2004. The county failed to take action to resolve this audit finding. Meanwhile, the amount in question continued to grow to in excess of \$100 million. As we have no practical means to compel the county to take action, we are bringing this matter to the attention of the appropriate staff members of the Legislature, the Legislative Analyst's Office, and the Department of Finance for review and consideration.

The county has disputed certain facts related to the audit finding. The SCO has an informal audit review process to resolve a dispute of facts. To request a review, the county should submit, in writing, a request for a review and all information pertinent to the disputed issues within 60 days after receiving the final report. The request and supporting documents should be submitted to Richard J. Chivaro, Chief Counsel, State Controller's Office, Post Office Box 942850, Sacramento, CA 94250-0001. In addition, provide a copy of the request letter to Steven Mar, Chief, Local Government Audits Bureau, Division of Audits, State Controller's Office, Post Office Box 942850, Sacramento, CA 95250-5874.

If you have any questions, please contact Mr. Mar at (916) 324-7226.

Sincerely,

*Original signed by*

JEFFREY V. BROWNFIELD  
Chief, Division of Audits

JVB/vb

cc: Pam Slater-Price, Chairwoman  
Board of Supervisors  
San Diego County  
Jody Martin, Principal Consultant  
Joint Legislative Budget Committee  
Peter Detwiler, Staff Director  
Senate Local Government Committee  
Elvia Dias, Committee Assistant  
Senate Local Government Committee  
Dixie Martineau-Petty, Secretary  
Assembly Local Government Committee  
Gayle Miller, Staff Director  
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Oksana Jaffe, Chief Consultant  
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Neil McCormick, Executive Director  
California Special Districts Association  
Richard J. Chivaro, Chief Counsel  
State Controller's Office

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# Audit Report

## Summary

The State Controller's Office (SCO) audited the methods employed by San Diego County to apportion and allocate property tax revenues for the period of July 1, 2003, through June 30, 2009.

Our audit disclosed that the county complied with California statutes, except that it computed the Fiscal Year (FY) 1978-79 base-year apportionment (SB 154 Split) in error, thus overstating the General Fund revenue base (noted in previous SCO audits). The cumulative effect of this error, as of June 30, 2009, is that the county's General Fund received approximately \$109,379,259 more in revenues, while the public schools and special districts did not receive approximately \$101,504,582 and \$7,874,677, respectively. In addition, the county included the Educational Revenue Augmentation Fund in the unitary and operating nonunitary tax apportionment computation during this audit period.

Prior to FY 2006-07, counties could not impose a fee, charge, or other levy on a city, nor reduce a city's allocation of ad valorem property tax revenue, in reimbursement for the services performed by the county under Revenue and Taxation Code sections 97.68 and 97.70. Pursuant to Revenue and Taxation Code section 97.75, for FY 2006-07 and thereafter, a county may impose a fee, charge, or other levy on a city for these services, but the fee, charge, or other levy cannot exceed the actual cost of providing the services.

A dispute has arisen between the counties and the cities regarding the application of Revenue and Taxation Code section 95.3 relating to the computation of Property Tax Administration Fees (PTAF). The counties generally contend that distribution factors for purposes of distributing PTAF to taxing agencies should be computed including amounts received by cities under Revenue and Taxation Code section 97.68, commonly known as the "Triple Flip," and section 97.70, commonly known as the "VLF Swap." The cities generally believe that the Triple Flip and the VLF Swap should be excluded from the computation.

We are aware of two legal actions that have been filed on this issue.

- In the first action, 47 cities in Los Angeles County filed suit against the county. On June 2, 2009, the court referee determined that the method used by Los Angeles County was correct.
- In the second action, filed in Fresno County, seven cities filed suit against the county. In this action, the court ruled that the method used by Fresno County was not in accordance with statute. This is the same method approved by the referee in Los Angeles County.

The SCO will make a determination on the computation of the PTAF at such time as appeals (if any) are resolved.

## Background

After the passage of Proposition 13 in 1978, the California State Legislature enacted new methods for allocating and apportioning property tax revenues to local government agencies and public schools. The main objective was to provide local government agencies with a property tax base that would grow as assessed property values increased. These methods have been further refined in subsequent laws passed by the Legislature.

The calculation of a county's base year (FY 1978-79) revenue amounts is the foundation from which all other property tax allocation and apportionment calculations are derived. Government Code section 26912 (Senate Bill [SB] 154, Chapter 292, Statutes of 1978) established the methodology to be employed for determining the base-year "split" of property tax revenues between the local government agencies and schools.

The split, or the "154 Split," is defined by a percentage of the total amount of revenue received in FY 1977-78 by local agencies and schools. The percentage was the first defining split of revenue for FY 1978-79.

One key law was Assembly Bill (AB) 8, which established the method of allocating property taxes for FY 1979-80 (base year) and subsequent fiscal years. The methodology is commonly referred to as the AB 8 process or the AB 8 system.

The property tax revenues that local government agencies receive each fiscal year are based on the amount received in the prior year, plus a share of the property tax growth within their boundaries. Property tax revenues are then apportioned and allocated to local agencies and schools using prescribed formulas and methods defined in the Revenue and Taxation Code.

The AB 8 base process involved numerous steps, including the transfer of revenues from schools to local agencies (AB 8 shift) and the development of the tax rate area annual tax increment apportionment factors (ATI factors), which determine the amount of property tax revenues to be allocated to each jurisdiction.

The total amount to be allocated to each jurisdiction is then divided by the total amount to be allocated to all entities to determine the AB 8 apportionment factor (percentage share) for each entity for the year. The AB 8 factors are computed each year for all entities, using the revenue amounts established in the prior year. These amounts are adjusted for growth annually, using ATI factors.

Subsequent legislation removed revenues generated by unitary and operating nonunitary property from the AB 8 system. This revenue is now allocated and apportioned under a separate system.

Other legislation established an Educational Revenue Augmentation Fund (ERAF) in each county. Most local government agencies are required to transfer a portion of their property tax revenues to the fund. The fund is subsequently allocated and apportioned to schools by the

county auditor according to instructions received from the county superintendent of schools or the State Chancellor of Community Colleges.

Revenues generated by the different types of property tax are apportioned and allocated to local agencies and schools using prescribed formulas and methods, as defined in the Revenue and Taxation Code. Taxable property includes land, improvements, and other properties that are accounted for on the property tax rolls maintained primarily by the county assessor. Tax rolls contain an entry for each parcel of land, including the parcel number, the owner's name, and the value. Following are the types of property tax rolls:

- *Secured Roll*—This roll contains property that, in the opinion of the assessor, has sufficient value to guarantee payment of the tax levies and that, if necessary, can be sold by the tax collector to satisfy unpaid tax levies.
- *Unsecured Roll*—This roll contains property that, in the opinion of the assessor, does not have sufficient “permanence” or have other intrinsic qualities to guarantee payment of taxes levied against it.
- *State-Assessed Roll*—This roll contains public utility and railroad properties, assessed as either unitary or nonunitary property by the State Board of Equalization.
- *Supplemental Roll*—This roll contains property that has been reassessed due to a change in ownership or the completion of new construction, where the resulting change in assessed value is not reflected in other tax rolls.

To mitigate problems associated with the apportionment and allocation of property taxes, legislation (SB 418) was enacted in 1985 that requires the State Controller to audit the counties' apportionment and allocation methods and report the results to the California State Legislature.

## **Objective, Scope, and Methodology**

Our audit objective was to review the county's apportionment and allocation of property tax revenues to local government agencies and public schools within its jurisdiction to determine whether the county complied with Revenue and Taxation Code requirements.

To meet the objective, we reviewed the systems for apportioning and allocating property tax revenues used by the county auditor and the subsystems used by the tax collector and the assessor.

We performed the following procedures:

- Conducted tests to determine whether the county correctly apportioned and allocated property tax revenue.
- Interviewed key personnel and reviewed supporting documentation to gain an understanding of the county's property tax apportionment and allocation processes.

- Reviewed apportionment and allocation reports prepared by the county showing the computations used to develop the property tax distribution factors.
- Reviewed tax rate area (TRA) reports to verify that the annual tax increment was computed properly.
- Reviewed county unitary and operating nonunitary reports and Board of Equalization reports and verified the computations used by the county to develop the unitary and operating nonunitary property tax distribution factors.
- Reviewed redevelopment agency (RDA) reports prepared by the county and verified the computations used to develop the project base amount and the tax increment distributed to the RDA.
- Reviewed property tax administration cost reports prepared by the county and verified administrative costs associated with procedures used for apportioning and allocating property tax to local government agencies and school districts.
- Reviewed ERAF reports prepared by the county and verified the computations used to determine the shift of property taxes from local agencies to the ERAF and, subsequently, to public schools.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. The audit covered the period of July 1, 2003, through June 30, 2009. However, we did not audit the county's financial statements. Our audit scope was limited to:

- Reviewing operational procedures and significant applicable controls over the apportionment and allocation process;
- Examining selected property tax apportionment and allocation records; and
- Reviewing related property tax revenue data used to determine the apportionment and allocation computation process.

We limited our review of the county's internal controls to gaining an understanding of the transaction flow in order to develop appropriate auditing procedures. We did not evaluate the effectiveness of all internal controls.

In addition, we tested transactions used to apportion and allocate property taxes and performed other procedures deemed necessary. This report relates solely to the method used by the county to apportion and allocate property taxes.



## Conclusion

Our audit disclosed that, except for the items discussed in the Findings and Recommendations section of this report, San Diego County complied with California statutes for the apportionment and allocation of property tax revenues for the period of July 1, 2003, through June 30, 2009. The county should correct the items discussed in the Findings and Recommendations section.

Prior to FY 2006-07, counties could not impose a fee, charge, or other levy on a city, nor reduce a city's allocation of ad valorem property tax revenue, in reimbursement for the services performed by the county under Revenue and Taxation Code sections 97.68 and 97.70. Pursuant to Revenue and Taxation Code section 97.75, for FY 2006-07 and thereafter, a county may impose a fee, charge, or other levy on a city for these services, but the fee, charge, or other levy cannot exceed the actual cost of providing the services.

A dispute has arisen between the counties and the cities regarding the application of Revenue and Taxation Code section 95.3 relating to the computation of PTAF. The counties generally contend that distribution factors for purposes of distributing PTAF to taxing agencies should be computed including amounts received by cities under Revenue and Taxation Code section 97.68, commonly known as the "Triple Flip," and section 97.70, commonly known as the "VLF Swap." The cities generally believe that the Triple Flip and the VLF Swap should be excluded from the computation.

We are aware of two legal actions that have been filed on this issue.

- In the first action, 47 cities in Los Angeles County filed suit against the county. On June 2, 2009, the court referee determined that the method used by Los Angeles County was correct.
- In the second action, filed in Fresno County, seven cities filed suit against the county. In this action, the court ruled that the method used by Fresno County was not in accordance with statute. This is the same method approved by the referee in Los Angeles County.

The SCO will make a determination on the computation of the PTAF at such time as appeals (if any) are resolved.

## Follow-up on Prior Audit Findings

Findings noted in our prior audit, issued June 9, 2004, have been satisfactorily resolved by the county, with the exception of Finding 1 in this report. This finding was also noted in our three previous audit reports (September 20, 1991; May 30, 1997; and June 9, 2004).

## Views of Responsible Official

We issued a draft audit report on May 28, 2010. Tracy M. Sandoval, Auditor and Controller, responded by letter dated June 29, 2010 (Attachment). She disagreed with the audit results.

## **Restricted Use**

This report is solely for the information and use of San Diego County, the California Legislature, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record.

*Original signed by*

JEFFREY V. BROWNFIELD  
Chief, Division of Audits

September 16, 2010

# Findings and Recommendations

## **FINDING 1— Distribution of the 1978-79 base-year apportionments (SB 154 split)**

As noted in the three previous SCO audits (issued on September 20, 1991; May 30, 1997; and June 9, 2004), the county computed the Fiscal Year (FY) 1978-79 base-year apportionment (SB 154 Split) in error, thus overstating the General Fund revenue base.

The county did not use the correct “split” factor (percent of local agencies vs. public schools) and apportionment factors computed from the FY 1977-78 revenues to apportion the FY 1978-79 property tax revenues. Our initial audit, dated September 20, 1991, disclosed that in FY 1978-79 the county General Fund received approximately \$694,500 more revenues, while public schools and special districts received approximately \$644,500 and \$50,000 less, respectively.

For FY 2008-09, based on the county’s own assessed valuation reports used to calculate its countywide growth rates, our calculation indicates that, for public schools, this amount has increased to \$8,314,033 (see Table 1). The cumulative effect of this finding is that the county’s General Fund received approximately \$109,379,259 more in revenues, while the public schools and special districts received approximately \$101,504,582 and \$7,874,677 less, respectively (see Table 2).

Requirements for the apportionment and allocation of the annual tax increment (ATI) are found in Revenue and Taxation Code sections 96 through 96.5. The annual increment of property tax, which is the change in assessed value from one year to the next, is allocated to tax rate area (TRAs) on the basis of each TRA’s share of the incremental growth in assessed valuations. The tax increment is then multiplied by the jurisdiction’s annual tax increment apportionment factors for each TRA. These factors were developed in the 1979-80 base year and are adjusted for jurisdictional changes. The tax increment is then added to the tax computed for the prior fiscal year to develop the apportionment for the current fiscal year.

### Recommendation

The county should correct the base-year amounts in the property tax system and reimburse all entities that have been impacted by this error.

### County's Response

Finding 1 of the 2010 Draft Audit is a finding that has been carried over for a number of audit periods since its inception. Finding 1 was first reported for the audit period covering fiscal years 1978-79 through 1989-90, in a report issued in 1991 ("1991 Audit"). It was carried over again for the audit period covering fiscal years 1990-91 through 1994-95 in a report issued in 1997 ("1997 Audit"), and the audit period that covered fiscal years 1995-96 through 2002-03 in an audit report issued in 2004 ("2004 Audit"). Finding 1 was again carried over for the current audit period covering fiscal years 2003-04 through 2008-09 in the 2010 Draft Audit. The County has consistently disputed Finding 1 each time it was re-issued in the aforementioned audits. The basis for the County's continued dispute is outlined below.

First, the Department of Finance audited the County and issued a report on March 25, 1982, and a follow-up report dated April 9, 1982 ("1982 Audit"), both of which are attached and we have previously provided, approving the County's calculation and distribution method. As noted in the March 25<sup>th</sup> letter, "[a] variety of information was reviewed on topics such as computation of the AB 8 adjusted tax base 1979/80 revenues" and "distribution of property tax revenue increment. . . ." The 1982 Audit concluded, "the information which was reviewed indicated that San Diego County's apportionment and allocation methods are generally in compliance with our interpretation of legal requirements." In its follow-up April 9<sup>th</sup> letter, the Department of Finance, having again reviewed its audit findings, confirmed that the County used a correct tax base. The County therefore continued to apply this approved methodology.

The SCO then audited the County's property tax revenue apportionment and allocation procedures for the period of July 1, 1978 through June 30, 1990 ("1990 Audit"). Concerning the 1978-1979 base year apportionment, the 1990 Audit noted,

"Many of the following issues have been noted in other counties and in some instances indicate a need for clarifying legislation. The type or quantity of issues presented do not necessarily indicate a good or bad processing system, but merely demonstrate the complexity of property tax allocation and apportionment. . . . The County did not use the correct "split" factor (percent of local agencies vs. school entities) and apportionment factors computed from the 1977/78 revenue to apportion the 1978/79 Property Tax Revenue. The split and apportionment factors were not off by a large amount, but the County General Fund received approximately \$694,500 more revenue and all other local agencies and schools received slightly less revenue than they should have."

The County disagreed and responded to the 1990 Audit as follows:

"I disagree with the statement that the County did not use the correct split factor to apportion the 1978/79 property tax revenue. The County of San Diego allocated the 1978/79 property tax pursuant to SB154 in that a three-year average was determined for local agencies and the prior year revenue was used for schools. Because of the amount of time that has elapsed from implementation to the audit, some of the microfilm records had

deteriorated to the point of being unreadable<sup>1</sup>. I feel it is inappropriate for a specific finding of this nature to be included in the audit findings when the evidence is so circumstantial in light of the whole balancing process. I am also concerned with the fact that when the Department of Finance audit was done in 1982, no findings in this area were noted. As noted in their audit report, a review of the allocation system as well as internal audit working papers indicated that the methods used to allocate property tax revenues were in compliance with their interpretation of legal requirements. At that time, the hard copies of the reports were available and reviewed by the audit staff. I am requesting that finding either be deleted from the audit report or be modified to one with no revenue impact to the County.

The Auditor's Reply to the County's Response was, in its entirety, as follows:

"The above audit finding was achieved using the Countys' [sic] own computations, reports, and workpapers that clearly indicate that the amount apportioned to the County General Fund in the 1978-79 fiscal year was not accurately derived from the "split percentage" and 3 year average revenue ratio."

Government Auditing Standards require that when an auditee's comments are inconsistent with the reports findings and the auditor disagrees with the auditee's comments that the auditor should explain their reasons for the disagreement and modify the report as necessary with sufficient and appropriate evidence. See GAO-07-162G, Section 5.37, 6.49 and 8.36. If there was evidence of any specific error, this was the opportunity to provide the appropriate evidence and explain the SCO's finding. Instead, the SCO simply denied the County's request to delete this finding from the 1990 Audit report and maintained its position regarding the finding despite the Department of Finance's earlier written confirmation asserting that the County's methods were in compliance with legal requirements.

The SCO then audited the County's property tax revenue apportionment and allocation procedures for the period of July 1, 1990 through June 30, 1995 ("1997 Audit"). Finding 1 was carried over without additional comment except a note related to growth. Similar to the 1990 Audit, the 1997 Audit does not identify any specific error in the split factors used by the County, nor does it articulate how the SCO believes things should have been done differently. The County continued to disagree with Finding 1. The SCO then audited the County's property tax revenue apportionment and allocation procedures for the period of July 1, 1995 through June 30, 2003 ("2004 Audit"). Finding 1 was again carried over. The 2004 Audit recommended that the County "correct the base year amounts in the system and reimburse all entities that have been impacted by this error." While the SCO continues to state the County general fund received approximately \$694,500 more in revenues than they should have received, at no time has the SCO pointed to the specific evidence of the alleged error.

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<sup>1</sup> The importance of this statement is that the \$694,500 figure, which was a figure determined by the SCO and not the County, could not be proved or disproved in 1990 due to the condition of the County's records.

The County's response in the 2004 Audit remained consistent with previous responses to the Finding. However, the County also raised the issue of the statute of limitations, which is three years. Civ. Proc. § 338, subd. (a). The 2004 Audit contends that this is a "legal issue" and that "the Legislature did not require the SCO to start performing the audits until after the (county-proposed) statute of limitations would have expired. The State would have had no chance to discover the error until the statute had expired, thus precluding the State from seeking a remedy."

The County continues to disagree with the SCO's Finding 1. The State, through its Department of Finance, had the opportunity to discover the alleged error during their audit in 1982, yet noted no such error. Further, the 2004 Audit implies that the statute of limitations runs anew if a different department within the State undertakes an audit concerning the same issue. We are unaware of any legal authority in support of this contention.

Given the lengthy history of Finding 1, the continuing lack of specifics with regard to any error, and the inability of either the SCO or the County to reconstruct what took place in 1978, the County has no basis to "correct" or change the apportionment factors even on a "going forward" basis. Although the 2010 Draft Audit attempts to quantify the amounts of the alleged error, the SCO amounts provided are based on sheer speculation as there is no evidence to show what different split factors might have been used or what the impact was on individual school districts and other agencies which may or may not have existed in 1978, not to mention jurisdictional changes of the districts and other agencies since 1978. The SCO has continued to carry over Finding 1 based on documentation which was reviewed in 1990 from records back in 1978. Even in 1991, the 1978 records were unreadable. The Department of Finance audit in 1982 was performed closest in time to the alleged error and, as indicated previously, the Department of Finance found the County's apportionment and allocation methods "generally in compliance with our interpretation of legal requirements."

As the alleged error occurred in 1978, the County's concern raised in response to the 2004 Audit as to the statute of limitations is particularly compelling and therefore must be given considerable weight in determining whether Finding 1 should even be included in the 2010 Audit Report. Additionally, as stated in the 2004 Audit, the SCO has conducted their audits outside the timeframe described in Government Code section 12468. Government Code section 12468, subdivision (b), requires the Controller to regularly audit counties' apportionment and allocation of property tax revenue on a three-year cycle for counties with a population greater than 200, 000 and less than 5,000,000. The 2004 Audit was on a nine-year cycle. The 2010 Draft Audit is on a six-year cycle. The County should have the opportunity to address any issues raised by the SCO within the three-year time frame.

Given the facts and circumstances provided and recognized Government Auditing Standards, unless the SCO can identify and support with "sufficient and appropriate evidence" the underlying basis for the original Finding 1 from the 1990 Audit, we believe the SCO has no choice but to remove Finding 1 from the 2010 Draft Audit Report.

SCO's Comment

Our finding and recommendation remain unchanged.

The county, in its response, has provided the history of this finding, one that stretches back over 20 years and relates to the county's actions more than 30 years ago.

The county notes in its response that it was audited by the Department of Finance (DOF) and that the DOF issued a report on March 25, 1982, and a follow-up report on April 9, 1982. However, the county does not state that the reports were draft reports and not final reports. The March 25, 1982, report states "If you like, your office may prepare a written response to the audit exception. This response should be received by May 1<sup>st</sup> to allow for reference or incorporation into the final report." The April 9, 1982, report dropped the exception noted in the earlier letter. It also included specific suggestions for the county. As the intended date for the final report appears to be after May 1, 1982, the reports referred to can only be considered drafts. In addition, while the county provided copies of the draft reports, it has not provided a copy of the final report.

On a related note, the March 25, 1982 report referred to above states, in part, "A variety of information was reviewed on topics such as computation of the AB8 adjusted base 1979-80 revenues, distribution of property tax revenue increment. . . ." No date earlier than 1979-80 is mentioned in the draft report. However, the audit finding is concerned with the fiscal year 1978-79 split factors. Our finding from the first audit states, in part, "**The County did not use the correct 'split' factor (percent of local agencies vs. school entities) and apportionment factors computed from the 1977/78 revenue to apportion the 1978/79 Property Tax Revenue** [emphasis added]." There is nothing in the DOF draft audit reports to indicate the DOF considered the computation of the 1978-79 split factors.

We acknowledge that the March 25, 1982 draft report states, "Again, the information which was reviewed indicated that San Diego County's allocation methods are generally in compliance with our interpretation of legal requirements." However, while the methods may be correct, if the revenue data being used is flawed, then the results emanating from the system will also be flawed.

The county further notes that in its response to the 2004 audit, in addition to its consistency with prior responses, it raised the issue of the statute of limitations. The county notes that the SCO responded that this was "a 'legal issue' and that 'the Legislature did not require the SCO to start performing the audits until after the (county-proposed) statute of limitations would have expired. . . . [and that] the State would have had no chance to discover the error . . . thus precluding the State from seeking a remedy.' " The county continues, "The State, through its Department of Finance, had the opportunity to discover the alleged error during their audit in 1982, yet noted no such error. Further, the 2004 Audit implies that the statute of limitations runs anew if a different department within the State undertakes an audit concerning the same issue. We are unaware of any legal authority in support of this

contention. . . . As the alleged error occurred in 1978, the County's concern raised in response to the 2004 Audit as to the statute of limitations is particularly compelling and therefore must be given considerable weight in determining whether Finding 1 should even be included in the 2010 Audit Report." We believe that more compelling is the fact that there is nothing in the 1982 DOF draft audit report to indicate that the DOF ever considered the issue, even though the county continues to hold out the draft audit report as justification for its position.

The county further states there is no basis to correct or change the apportionment factors even on a prospective basis, indicating that the quantification of the "alleged error" is based on sheer speculation because "there is no evidence to show what different split factors might have been used or what the impact was on individual school districts and other agencies which may or may not have existed in 1978, not to mention jurisdictional changes of the districts and other agencies since 1978."

The amount is not speculation. Our finding is based on documentation reviewed during the first audit that determined that the county made an error in the computation of the split factor. The error resulted in the County receiving more property tax revenue than it was entitled to at the expense of schools and special districts. The computation of the amount currently due is based on the original documented error and adjusted by growth percentages taken from the county's own records. The county's responsibility is not negated by subsequent jurisdictional changes. The county has a fiduciary responsibility to allocate and apportion property tax revenues correctly.



**FINDING 2—  
ERAF included in the  
unitary and operating  
nonunitary  
apportionment**

The county included the Educational Revenue Augmentation Fund (ERAF) in the unitary and operating nonunitary tax apportionment computation.

Requirements for the apportionment and allocation of unitary and operating nonunitary property taxes are found in Revenue and Taxation Code section 100.

Unitary properties are those properties on which the Board of Equalization “may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in the primary function of the assessee” (i.e., public utilities and railroads). The Revenue and Taxation Code further states, “Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee.”

In FY 1988-89, the Legislature established a separate system for apportioning and allocating the unitary and operating nonunitary property taxes. The Legislature established the unitary and operating nonunitary base year and developed formulas to compute the distribution factors for the fiscal years that followed.

Recommendation

The county should not include the ERAF in future unitary and operating nonunitary tax apportionment computations, as the ERAF does not qualify as a “taxing jurisdiction” under Revenue and Taxation Code section 100. Thus, the ERAF is not eligible to share and its amount should be distributed proportionately among all taxing jurisdictions that contributed to the fund.

County’s Response

With regard to Finding 2, consistent with the majority of counties in the State, the County did include ERAF in the unitary and operating nonunitary apportionments in accordance with unitary and nonunitary allocation guidelines. The State Auditor’s Association recommended that County Auditors make no changes in their allocation methodology and stay consistent in following the Property Tax Manager’s Reference Manual. Until the legislature clarifies this issue, we do not intend to change our position.

SCO’s Comment

Our finding and recommendation remain unchanged.

The ERAF is a fund—an accounting entity, not a taxing jurisdiction. Revenue and Taxation Code section 100 requires that taxes from unitary and operating nonunitary property be allocated to taxing jurisdictions. As the ERAF is not a taxing jurisdiction, it is not eligible to receive unitary and operating nonunitary taxes.

Revenue and Taxation Code section 100(c) states, “The property tax revenue derived from the assessed value assigned to the countywide tax rate area pursuant to subdivision (a) and pursuant to paragraph (2) of subdivision (a) of Section 100.1 by the use of the tax rate determined in paragraph (1) of subdivision (b) shall be allocated as follows: (1) For the 1988-89 fiscal year and each fiscal year thereafter, each taxing jurisdiction shall be allocated an amount of property tax revenue. . . .”

Revenue and Taxation Code section 95 (a) defines a local agency as a “city, county, and special district.” In addition, Revenue and Taxation Code section 95(b) defines a jurisdiction as a “local agency, school district, community college district, or county superintendent of schools. A jurisdiction as defined in this subdivision is a ‘district’ for purposes of section 1 of Article XIII A of the California Constitution.” Furthermore, Revenue and Taxation Code section 100(e)(3) includes a redevelopment agency as a taxing jurisdiction, demonstrating that the Legislature knows how to include non-taxing entities in the definition of a taxing jurisdiction. In this case, it omitted the ERAF from the definition of taxing jurisdiction.

Finally, the Property Tax Manager’s Reference Manual is a guide, not a statute. The SCO performs audits according to applicable statutes. The ERAF is a fund, an accounting entity, and not a taxing jurisdiction. Revenue and Taxation Code section 100 requires that taxes from unitary and operating nonunitary property be allocated to taxing jurisdictions. Since the ERAF is not a taxing jurisdiction, it is not eligible to receive unitary and operating nonunitary taxes.

**TABLE 1**  
**San Diego County**  
**AB 8 (1%) Property Tax Revenue for Schools**  
**Fiscal Year 2008-09**

Fund Number	Description	AB 8 Share / AB 8 Factor	AB 8 Apportioned Revenue (1)	SCO Computed Growth Revenue (2)	Combined Apportioned and Growth Revenue (3)
<b>ELEMENTARY SCHOOL DISTRICTS</b>					
4103	Alpine Union	0.00108199	\$ 4,313,479	\$ 19,094	\$ 4,332,573
4109	Bonsall Union	0.00132897	5,298,111	23,452	5,321,563
4112	Cajon Valley Union	0.00684448	27,286,431	120,783	27,407,213
4115	Cardiff	0.00135658	5,408,171	23,939	5,432,111
4117	Chula Vista	0.02115192	84,324,882	373,262	84,698,144
4120	Dehesa	0.00018987	756,937	3,351	760,287
4121	Del Mar Union	0.00817912	32,607,141	144,335	32,751,476
4126	Encinitas Union	0.00844536	33,668,543	149,033	33,817,576
4127	Escondido Union	0.00895911	35,716,682	158,099	35,874,780
4130	Fallbrook Union	0.00221056	8,812,696	39,009	8,851,705
4141	Jamul-Dulzura union	0.00070065	2,793,222	12,364	2,805,586
4143	Julian Union	0.00042292	1,686,031	7,463	1,693,494
4148	Lakeside Union	0.00191885	7,649,737	33,861	7,683,598
4149	La Mesa-Spring Valley	0.00616511	24,578,020	108,794	24,686,814
4151	Lemon Grove	0.00122876	4,898,617	21,684	4,920,301
4160	National	0.00113753	4,534,910	20,074	4,554,983
4176	Rancho Santa Fe	0.00206177	8,219,504	36,383	8,255,887
4181	Solana Beach	0.00716990	28,583,748	126,525	28,710,273
4185	San Pasqual Union	0.00029375	1,171,081	5,184	1,176,265
4187	Santee	0.00271442	10,821,409	47,901	10,869,309
4188	San Ysidro	0.00375365	14,964,405	66,240	15,030,644
4190	South Bay Union	0.00217571	8,673,735	38,394	8,712,129
4191	Spencer Valley	0.00004554	181,569	804	182,372
4197	Vallecitos	0.00018205	725,785	3,213	728,998
<b>HIGH SCHOOL DISTRICTS</b>					
4219	Escondido Union	0.00710586	28,328,430	125,395	28,453,825
4225	Fallbrook Union	0.00226444	9,027,470	39,960	9,067,430
4231	Grossmont Union	0.02113108	84,241,802	372,894	84,614,696
4235	Julian Union	0.00035810	1,427,613	6,319	1,433,933
4255	San Dieguito Union	0.01993148	79,459,455	351,725	79,811,180
4259	Sweetwater Union	0.01755886	70,000,688	309,856	70,310,545
<b>UNIFIED SCHOOL DISTRICTS</b>					
4310	Borrego Springs	0.00054781	2,183,923	9,667	2,193,590
4311	Coronado	0.00078688	3,137,014	13,886	3,150,900
4312	Carlsbad	0.01532499	61,095,080	270,436	61,365,516
4315	Mt. Empire	0.00141407	5,637,356	24,954	5,662,310
4317	Oceanside	0.01174409	46,819,343	207,245	47,026,588
4320	Poway	0.02922016	116,489,975	515,640	117,005,615
4325	Ramona	0.00470680	18,764,286	83,060	18,847,345
4328	San Diego	0.13553306	540,320,251	2,391,714	542,711,965
4329	San Marcos	0.00861520	34,345,627	152,030	34,497,657
4336	Valley Center-Pauma	0.00415079	16,547,666	73,248	16,620,914
4338	Vista	0.01409308	56,183,904	248,697	56,432,600
4339	Warner	0.00026949	1,074,343	4,756	1,079,098
<b>COMMUNITY COLLEGE DISTRICTS</b>					
4430	Grossmount-Cuyanaca	0.00833126	33,213,676	147,019	33,360,696
4440	Palomar	0.01387304	55,306,679	244,814	55,551,492
4450	Mira Costa	0.01893635	75,492,233	334,164	75,826,397
4455	San Diego	0.01952121	77,823,857	344,485	78,168,343
4460	Southwestern	0.00553451	22,064,063	97,666	22,161,729

**COUNTY OFFICE OF EDUCATION FUNDS**

4535-01 County School Service	0.00680763	27,139,488	120,132	27,259,620
4535-04 County School Service - Capital Outlay	0.00170874	6,812,122	30,154	6,842,275
4535-12 Trainable Mentally Retarded Minors Elem Comp	0.00080854	3,223,351	14,268	3,237,619
4535-13 Physically Handicapped Minors Elem Comp	0.00119026	4,745,124	21,004	4,766,128
4535-14 Educable Mentally Retarded Minors	0.00008442	336,551	1,490	338,041
4535-15 Children's Institutions Tuition	0.00144386	5,756,144	25,479	5,781,623
4535-16 Regional Occupational Centers	0.00433772	17,292,894	76,547	17,369,440
4535-17 Trainable Mentally Retarded Minors High Comp	0.00078238	3,119,070	13,806	3,132,876
4535-18 Physically Handicapped Minors High Comp	0.00112432	4,482,238	19,841	4,502,078
4535-19 Chula Vista Project (19/84601)	0.00002242	89,380	396	89,776
4535-20 Vista Project (19/85701)	0.00007073	281,956	1,248	283,204
4535-21 Oceanside Project (19/85001)	0.00002051	81,771	362	82,133
4535-22 Chula Vista Project (19/84602)	0.00003197	127,453	564	128,017
4535-23 Autistic Pupils Minors Elem Comp	0.00003613	144,025	638	144,662
4535-24 Carlsbad Project (19/86001)	0.00004678	186,493	826	187,319
4535-28 Autistic Pupils Minors High School Comp	0.00003402	135,638	600	136,238
4535-33 Development Centers for Handicapped EC56811 Elm	0.00017385	693,067	3,068	696,134
4535-38 Development Centers for Handicapped EC56811 High	0.00172580	688,003	30,455	718,457
5477 Alpine Union Co School Bldg Aid	0.00000051	2,038	9	2,047
5478 Cajon Valley Union Co School Bldg Aid	0.00000014	547	2	549
5479 Dehesa Co School Bldg Aid	0.00000024	958	4	962
5485 Coronado Co School Bldg Aid	0.00000007	288	1	290
5486 Lakeside Union Co School Bldg Aid	0.00000558	22,229	98	22,327
5487 La Mesa-Spring Valley Co School Bldg Aid	0.00000291	11,606	51	11,657
5488 Lemon Grove Co School Bldg Aid	0.00000215	8,557	38	8,595
5491 Jamul-Dulzura Union Co School Bldg Aid	0.00000087	3,459	15	3,474
5492 Mountain Empire Unified Co School Bldg Aid	0.00000064	2,567	11	2,578
5495 Santee Co School Bldg Aid	0.00000249	9,910	44	9,954
5496 Ramona Unified Co School Bldg Aid	0.00000077	3,083	14	3,096
<b>TOTALS</b>	<b>0.47113763</b>	<b>\$ 1,872,059,586</b>	<b>\$ 8,314,033</b>	<b>\$ 1,880,373,619</b>

(1) AB 8 share/apportionment factors and net revenues as reported by San Diego County AB 8 worksheets for FY 2008-09

(2) Represents total additional property tax revenues resulting from the SB 154 base year split error

(3) Total of the apportioned revenues and growth

**TABLE 2**  
**San Diego County**  
**Growth Calculation for the SB 154 Base-Year Split**  
**Fiscal Year 2008-09**

Year Ending June 30	Base Amount	Countywide Growth Percentage (1)	Growth Amount	Base Plus Growth	Cumulative Amount	School Growth	School Amount	School Cumulative	Special District Growth	Special District Amount	Special District Cumulative	Cumulative Total (Special Districts Plus Schools)
1979	\$ 694,500		\$ -	\$ 694,500	\$ 694,500	\$ -	\$ 644,500	\$ 644,500	\$ -	\$ 50,000	\$ 50,000	\$ 694,500
1980	694,500	0.20728851	143,962	838,462	1,532,962	133,597	778,097	1,422,597	10,364	60,364	110,364	1,532,962
1981	838,462	0.13781590	115,553	954,015	2,486,977	107,234	885,332	2,307,929	8,319	68,684	179,048	2,486,977
1982	954,015	0.12827040	122,372	1,076,387	3,563,364	113,562	998,893	3,306,823	8,810	77,494	256,542	3,563,364
1983	1,076,387	0.12527949	134,849	1,211,236	4,774,601	125,141	1,124,034	4,430,857	9,708	87,202	343,744	4,774,601
1984	1,211,236	0.08916454	107,999	1,319,236	6,093,836	100,224	1,224,258	5,655,115	7,775	94,977	438,721	6,093,836
1985	1,319,236	0.10876160	143,482	1,462,718	7,556,554	133,152	1,357,411	7,012,526	10,330	105,307	544,028	7,556,554
1986	1,462,718	0.11741915	171,751	1,634,469	9,191,023	159,386	1,516,797	8,529,323	12,365	117,672	661,701	9,191,023
1987	1,634,469	0.12800495	209,220	1,843,689	11,034,712	194,157	1,710,954	10,240,277	15,063	132,735	794,436	11,034,712
1988	1,843,689	0.11512279	212,251	2,055,940	13,090,652	196,970	1,907,924	12,148,201	15,281	148,016	942,452	13,090,652
1989	2,055,940	0.10564695	217,204	2,273,144	15,363,796	201,566	2,109,490	14,257,691	15,637	163,653	1,106,105	15,363,796
1990	2,273,144	0.11266628	256,107	2,529,250	17,893,046	237,668	2,347,159	16,604,850	18,438	182,091	1,288,196	17,893,046
1991	2,529,250	0.12919182	326,758	2,856,009	20,749,055	303,234	2,650,392	19,255,242	23,525	205,616	1,493,812	20,749,055
1992	2,856,009	0.07336902	209,543	3,065,551	23,814,606	194,457	2,844,849	22,100,091	15,086	220,702	1,714,514	23,814,606
1993	3,065,551	0.03830007	117,411	3,182,962	26,997,568	108,958	2,953,807	25,053,898	8,453	229,155	1,943,669	26,997,568
1994	3,182,962	0.01139148	36,259	3,219,221	30,216,788	33,648	2,987,455	28,041,354	2,610	231,765	2,175,435	30,216,788
1995	3,219,221	0.00797825	25,684	3,244,904	33,461,693	23,835	3,011,290	31,052,644	1,849	233,614	2,409,049	33,461,693
1996	3,244,904	0.01072018	34,786	3,279,690	36,741,383	32,282	3,043,572	34,096,215	2,504	236,119	2,645,168	36,741,383
1997	3,279,690	0.00233599	7,661	3,287,352	40,028,735	7,110	3,050,681	37,146,897	552	236,670	2,881,838	40,028,735
1998	3,287,352	0.02542100	83,568	3,370,919	43,399,654	77,551	3,128,233	40,275,129	6,016	242,687	3,124,525	43,399,654
1999	3,370,919	0.07080473	238,677	3,609,596	47,009,251	221,494	3,349,726	43,624,855	17,183	259,870	3,384,395	47,009,251
2000	3,609,596	0.10273185	370,821	3,980,417	50,989,668	344,124	3,693,850	47,318,705	26,697	286,567	3,670,962	50,989,668
2001	3,980,417	0.08401471	334,414	4,314,831	55,304,498	310,338	4,004,188	51,322,893	24,076	310,643	3,981,605	55,304,498
2002	4,314,831	0.09588408	413,724	4,728,554	60,033,052	383,938	4,388,125	55,711,018	29,786	340,429	4,322,034	60,033,052
2003	4,728,554	0.08568815	405,181	5,133,735	65,166,788	376,010	4,764,136	60,475,154	29,171	369,599	4,691,633	65,166,788
2004	5,133,735	0.09506591	488,043	5,621,778	70,788,566	452,907	5,217,043	65,692,197	35,136	404,736	5,096,369	70,788,566
2005	5,621,778	0.10124763	569,192	6,190,970	76,979,536	528,213	5,745,256	71,437,453	40,979	445,714	5,542,083	76,979,536
2006	6,190,970	0.13225917	818,813	7,009,783	83,989,319	759,863	6,505,119	77,942,571	58,950	504,664	6,046,747	83,989,319
2007	7,009,783	0.11963734	838,632	7,848,414	91,837,733	778,255	7,283,374	85,225,945	60,377	565,041	6,611,788	91,837,733
2008	7,848,414	0.09353224	734,080	8,582,494	100,420,227	681,230	7,964,604	93,190,549	52,850	617,890	7,229,678	100,420,227
2009	8,582,494	0.04387270	376,537	8,959,031	109,379,259	349,429	8,314,033	101,504,582	27,109	644,999	7,874,677	109,379,259

(1) (Current Assessed Value - Prior Assessed Value)/Prior Assessed Value Based on County Assessor's Assessed Values

**Attachment—  
County's Response to  
Draft Audit Report**

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## County of San Diego

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June 29, 2010

Steven Mar  
Chief, Local Government Audits Bureau  
State Controller's Office  
Division of Audits  
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Sacramento, CA 94250-5847

Dear Mr. Mar:

**STATE CONTROLLER'S DRAFT AUDIT OF COUNTY OF SAN DIEGO PROPERTY  
TAX REVENUES FOR THE PERIOD OF JULY 1, 2003 THROUGH JUNE 30, 2009  
("2010 DRAFT AUDIT")**

This letter is in response to the May 28, 2010 letter from Jeffrey Brownfield of the State Controller's Office ("SCO") to the County of San Diego's ("County") Assistant Chief Financial Officer/Auditor and Controller Tracy Sandoval and the County's receipt of the 2010 Draft Audit.

The County disputes both issues which are addressed in the 2010 Draft Audit. The first issue involves the fact that the County included the Educational Revenue Augmentation Fund ("ERAF") in the unitary and operating nonunitary tax apportionment computation during this audit period ("Finding 2").

With regard to Finding 2, consistent with the majority of counties in the State, the County did include ERAF in the unitary and operating nonunitary apportionments in accordance with unitary and nonunitary allocation guidelines. The State Auditor's Association recommended that County Auditors make no changes in their allocation methodology and stay consistent in following the Property Tax Manager's Reference Manual. Until the legislature clarifies this issue, we do not intend to change our position.

The remainder of this correspondence focuses on Finding 1 of the 2010 Draft Audit which deals with the County's calculation and distribution of the fiscal year 1978-79 base year apportionments, commonly referred to as the SB 154 Split ("Finding 1").

Finding 1 of the 2010 Draft Audit is a finding that has been carried over for a number of audit periods since its inception. Finding 1 was first reported for the audit period covering fiscal years 1978-79 through 1989-90, in a report issued in 1991 ("1991 Audit"). It was carried over again for the audit period covering fiscal years 1990-91 through 1994-95 in a report issued in 1997 ("1997 Audit"), and the audit period that covered fiscal years 1995-96 through 2002-03 in an audit report issued in 2004 ("2004 Audit"). Finding 1 was again carried over for the current audit period covering fiscal years 2003-04 through 2008-09 in the 2010 Draft Audit. The County has consistently disputed Finding 1 each time it was re-issued in the aforementioned audits. The basis for the County's continued dispute is outlined below.

First, the Department of Finance audited the County and issued a report on March 25, 1982, and a follow-up report dated April 9, 1982 ("1982 Audit"), both of which are attached and we have previously provided, approving the County's calculation and distribution method. As noted in the March 25<sup>th</sup> letter, "[a] variety of information was reviewed on topics such as computation of the AB 8 adjusted tax base 1979/80 revenues" and "distribution of property tax revenue increment . . . ." The 1982 Audit concluded, "the information which was reviewed indicated that San Diego County's apportionment and allocation methods are generally in compliance with our interpretation of legal requirements." In its follow-up April 9<sup>th</sup> letter, the Department of Finance, having again reviewed its audit findings, confirmed that the County used a correct tax base. The County therefore continued to apply this approved methodology.

The SCO then audited the County's property tax revenue apportionment and allocation procedures for the period of July 1, 1978 through June 30, 1990 ("1990 Audit"). Concerning the 1978/1979 base year apportionment, the 1990 Audit noted,

"Many of the following issues have been noted in other counties and in some instances indicate a need for clarifying legislation. The type or quantity of issues presented do not necessarily indicate a good or bad processing system, but merely demonstrate the complexity of property tax allocation and apportionment. . . . The County did not use the correct "split" factor (percent of local agencies vs. school entities) and apportionment factors computed from the 1977/78 revenue to apportion the 1978/79 Property Tax Revenue. The split and apportionment factors were not off by a large amount, but the County General Fund received approximately \$694,500 more revenue and all other local agencies and schools received slightly less revenue than they should have."

The County disagreed and responded to the 1990 Audit as follows:

"I disagree with the statement that the County did not use the correct split factor to apportion the 1978/79 property tax revenue. The County of San Diego allocated the 1978/79 property tax pursuant to SB154 in that a three-year average was determined for local agencies and the prior year revenue was used for schools. Because of the amount of time that has elapsed from



implementation to the audit, some of the microfilm records had deteriorated to the point of being unreadable<sup>1</sup>. I feel it is inappropriate for a specific finding of this nature to be included in the audit findings when the evidence is so circumstantial in light of the whole balancing process. I am also concerned with the fact that when the Department of Finance audit was done in 1982, no findings in this area were noted. As noted in their audit report, a review of the allocation system as well as internal audit working papers indicated that the methods used to allocate property tax revenues were in compliance with their interpretation of legal requirements. At that time, the hard copies of the reports were available and reviewed by the audit staff. I am requesting that finding either be deleted from the audit report or be modified to one with no revenue impact to the County."

The Auditor's Reply to the County's Response was, in its entirety, as follows:

"The above audit finding was achieved using the Countys' [sic] own computations, reports, and workpapers that clearly indicate that the amount apportioned to the County General Fund in the 1978-79 fiscal year was not accurately derived from the "split percentage" and 3 year average revenue ratio."

Government Auditing Standards require that when an auditee's comments are inconsistent with the reports findings and the auditor disagrees with the auditee's comments that the auditor should explain their reasons for the disagreement and modify the report as necessary with sufficient and appropriate evidence. See GAO-07-162G, Section 5.37, 6.49 and 8.36. If there was evidence of any specific error, this was the opportunity to provide the appropriate evidence and explain the SCO's finding. Instead, the SCO simply denied the County's request to delete this finding from the 1990 Audit report and maintained its position regarding the finding despite the Department of Finance's earlier written confirmation asserting that the County's methods were in compliance with legal requirements.

The SCO then audited the County's property tax revenue apportionment and allocation procedures for the period of July 1, 1990 through June 30, 1995 ("1997 Audit"). Finding 1 was carried over without additional comment except a note related to growth. Similar to the 1990 Audit, the 1997 Audit does not identify any specific error in the split factors used by the County, nor does it articulate how the SCO believes things should have been done differently. The County continued to disagree with Finding 1. The SCO then audited the County's property tax revenue apportionment and allocation procedures for the period of July 1, 1995 through June 30, 2003 ("2004 Audit"). Finding 1 was again carried over. The 2004 Audit recommended that the County "correct the

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<sup>1</sup> The importance of this statement is that the \$694,500 figure, which was a figure determined by the SCO and not the County, could not be proved or disproved in 1990 due to the condition of the County's records.

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base year amounts in the system and reimburse all entities that have been impacted by this error." While the SCO continues to state the County general fund received approximately \$694,500 more in revenues than they should have received, at no time has the SCO pointed to the specific evidence of the alleged error.

The County's response in the 2004 Audit remained consistent with previous responses to the Finding. However, the County also raised the issue of the statute of limitations, which is three years. Civ. Proc. § 338, subd. (a). The 2004 Audit contends that this is a "legal issue" and that "the Legislature did not require the SCO to start performing the audits until after the (county-proposed) statute of limitations would have expired. The State would have had no chance to discover the error until the statute had expired, thus precluding the State from seeking a remedy."

The County continues to disagree with the SCO's Finding 1. The State, through its Department of Finance, had the opportunity to discover the alleged error during their audit in 1982, yet noted no such error. Further, the 2004 Audit implies that the statute of limitations runs anew if a different department within the State undertakes an audit concerning the same issue. We are unaware of any legal authority in support of this contention.

Given the lengthy history of Finding 1, the continuing lack of specifics with regard to any error, and the inability of either the SCO or the County to reconstruct what took place in 1978, the County has no basis to "correct" or change the apportionment factors even on a "going forward" basis. Although the 2010 Draft Audit attempts to quantify the amounts of the alleged error, the SCO amounts provided are based on sheer speculation as there is no evidence to show what different split factors might have been used or what the impact was on individual school districts and other agencies which may or may not have existed in 1978, not to mention jurisdictional changes of the districts and other agencies since 1978. The SCO has continued to carry over Finding 1 based on documentation which was reviewed in 1990 from records back in 1978. Even in 1991, the 1978 records were unreadable. The Department of Finance audit in 1982 was performed closest in time to the alleged error and, as indicated previously, the Department of Finance found the County's apportionment and allocation methods "generally in compliance with our interpretation of legal requirements."

As the alleged error occurred in 1978, the County's concern raised in response to the 2004 Audit as to the statute of limitations is particularly compelling and therefore must be given considerable weight in determining whether Finding 1 should even be included in the 2010 Audit Report. Additionally, as stated in the 2004 Audit, the SCO has conducted their audits outside the timeframe described in Government Code section 12468. Government Code section 12468, subdivision (b), requires the Controller to regularly audit counties' apportionment and allocation of property tax revenue on a

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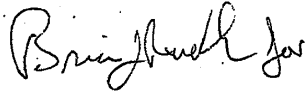
three-year cycle for counties with a population greater than 200,000 and less than 5,000,000. The 2004 Audit was on a nine-year cycle. The 2010 Draft Audit is on a six-year cycle. The County should have the opportunity to address any issues raised by the SCO within the three-year time frame.

Given the facts and circumstances provided and recognized Government Auditing Standards, unless the SCO can identify and support with "sufficient and appropriate evidence" the underlying basis for the original Finding 1 from the 1990 Audit, we believe the SCO has no choice but to remove Finding 1 from the 2010 Draft Audit Report.

Please contact the undersigned at (619) 531-5413 with any questions regarding this letter.

Thank you very much for your attention to this matter.

Sincerely,



TRACY M. SANDOVAL  
Assistant Chief Financial Officer/Auditor and Controller

AFC:BR:ld

Attachments

STATE OF CALIFORNIA  
**DEPARTMENT OF FINANCE**  
SACRAMENTO



March 25, 1982

Rod Calvao  
Auditor Controller  
San Diego County  
1600 Pacific Highway  
San Diego, CA 92101

**AUDIT OF PROPERTY TAX ALLOCATIONS**

San Diego County's allocation of property tax revenues was reviewed from February 24th to February 26th and March 2nd to March 4th as part of the Department of Finance's audit required by AB 777 (Chap. 100, Stat. of 1981).

A variety of information was reviewed on topics such as computation of the AB 8 adjusted base 1979-80 revenues, distribution of property tax revenue increment, handling of jurisdictional changes, use of the Special District Augmentation Fund, and allocation of community redevelopment increment. Descriptive, factual information on San Diego County's allocation system may be included within the final report to the State Legislature.

A review of the allocation system as well as internal audit working papers indicated that the methods used to allocate property tax revenues from 1979-80 through 1981-82 were generally in compliance with our interpretation of legal requirements.

One audit exception is noted. In 1981-82 the County appears to be undercharging debt funds and overcharging the funds receiving a share of the one percent property tax revenues. This undercharging and overcharging has occurred as part of the County's AB 8/SB 180 process of determining the amount of community redevelopment increment to be charged to the funds of the taxing districts within the tax rate areas that are part of a community redevelopment project. The finding has been previously noted by your office's internal audit staff with respect to the 1980-81 fiscal year.

The undercharging of debt funds specifically resulted from not making the estimated business inventories assessed valuation adjustments for debt funds as required by Government Code Section 16114. While the size of the 16114 adjustments have not covered the full reduction in assessed valuations resulting from nonassessment of business inventories, the adjustments should still be applied to debt funds since local claims against the State for the business inventories subvention cover ad valorem tax losses (both debt service and one percent).

The undercharging of debt funds has led to an overcharging of the one percent funds in order to make up the totals due the redevelopment agencies. We estimate that the undercharging/overcharging amounts to \$196,800 for 1981-82.

Rod Calvao

March 25, 1982

In addition, the following finding--although not the subject of an exception--may be analyzed in the report for informational purposes. Specifically, San Diego County appears to have followed the Ventura/Ventura models' handling of redevelopment agencies in computing the base values for the first year--1979-80. As a result, the redevelopment increment was excluded in computing the base revenues of the taxing districts, while the incremental assessed valuation of the redevelopment projects was included in the base assessed valuations which were used to distribute each taxing district's base revenues across tax rate areas.

Again, the information which was reviewed indicated that San Diego County's allocation methods are generally in compliance with our interpretation of legal requirements.

If you like, your office may prepare a written response to the audit exception. This response should be received by May 1st to allow for reference or incorporation into the final report.

Any questions should be directed to Kerry M. Adlfinger (916) 322-6640.



Richard L. Cutting, Chief  
Financial and Performance Accountability Unit  
and Program Evaluation Unit  
1025 "P" Street, Room 283  
Sacramento, CA 95814

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DEPARTMENT OF FINANCE  
SACRAMENTO

April 9, 1982

Rod Calvao  
Auditor-Controller  
San Diego County  
1600 Pacific Highway  
San Diego, CA 92101

AUDIT OF PROPERTY TAX ALLOCATIONS--AMENDMENT TO LETTER OF MARCH 25, 1982

In the attached March 25th letter, we stated that:

One audit exception is noted. In 1981-82 the County appears to be undercharging debt funds and overcharging the funds receiving a share of the one percent property tax revenues. This undercharging and overcharging has occurred as part of the County's AB 8/SB 180 process of determining the amount of community redevelopment increment to be charged to the funds of the taxing districts within the tax rate areas that are part of a community redevelopment project. The finding has been previously noted by your office's internal audit staff with respect to the 1980-81 fiscal year.

The undercharging of debt funds specifically resulted from not making the estimated business inventories assessed valuation adjustments for debt funds as required by Government Code Section 16114. While the size of the 16114 adjustments have not covered the full reduction in assessed valuations resulting from nonassessment of business inventories, the adjustments should still be applied to debt funds since local claims against the State for the business inventories subvention cover ad valorem tax losses (both debt service and one percent).

The undercharging of debt funds has led to an overcharging of the one percent funds in order to make up the totals due the redevelopment agencies. We estimate that the undercharging/overcharging amounts to \$196,800 for 1981-82.

My staff advise me that the audit exception should be dropped. Subsequent to preparation of the March 25th letter, it has been brought to the attention of my staff that Chapter 610, Statutes of 1980, appears to predicate the business inventories claim against the State upon the general levy (as opposed to debt

Rod Calvao

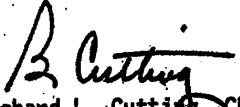
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April 9, 1982

service) for 1979-80, as adjusted by the State Reimbursement For Inventory Tax Factor. At the same time, the formula in Government Code Section 16114 appears to depress the estimated assessed valuation for business inventories so that both the general levy (i.e., one percent) and debt rates may be applied in determining how much of the subvention is owed to redevelopment agencies.

As a result of this situation, it becomes unclear whether San Diego's apparent undercharging of debt funds is actually incorrect. While Government Code Section 16114 appears designed to allow credit for debt rates, it would be appropriate to charge debt funds only if revenue from the subvention has actually been allocated to such funds. Information collected during the Finance review was insufficient to determine if the debt funds received such allocation. As a result, we suggest that this matter be referred to your property tax and audit staff for resolution. We specifically suggest that attention be given to whether the business inventories subvention due redevelopment agencies was allocated to debt funds of the taxing districts within redevelopment zones and, if not, whether it should have been.

Any questions should be directed to Kerry M. Adlfinger (916) 322-6640.

  
Richard L. Cutting, Chief  
Financial and Performance Accountability Unit  
and Program Evaluation Unit  
1025 "P" Street, Room 283  
Sacramento, CA 95814

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